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Trade Policy: Where Will America Lead?

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Following is an address by Douglas W. McMinn, Assistant Secretary for Economic and Business Affairs, before the Baltimore Council on Foreign Affairs, Baltimore, Maryland, July 2, 1986.

The question I want to put before you tonight is: where will America lead? Will America lead to more open trade among nations? Will America lead to greater economic and political freedom around the world? When put to the test, what course will we steer for ourselves and the world?

Economic and Political Freedom

As we approach the Fourth of July, it is appropriate to remind ourselves of the fundamental principles on which our nation is built. The Founding Fathers understood that political and economic freedom were inseparable and believed that human freedom and private initiative would bring America progress and prosperity. We have grown from a weak colony to a prosperous nation by remaining true to the vision of the Founding Fathers.

Two hundred and ten years have passed since the signing of the Declaration of Independence. In their wildest dreams the Founding Fathers could never have imagined how successful America's experiment with freedom would be.

Our political and economic freedom serves as an inspiring example to the rest of the world. Countries in Asia, Africa, Latin America, and even Europe are embracing democracy. In a quieter but equally important revolution, nations all over the world are rejecting state-controlled, interventionist economic systems and adopting market-oriented economic regimes.

One of the fundamental principles of economic freedom is free and open trade. History has taught us that the freer the flow of trade, the greater world economic progress and the greater the incentive for peaceful relations among nations.

Trade

At the moment, one of the top issues in Washington is trade policy. Recently, the House of Representatives passed an omnibus trade bill. The Senate has now taken up trade legislation.

It is within the context of economic and political freedom that we need to examine today's trade policy debate. When the trade bills are debated on Capitol Hill, the vision of the upcoming November elections is clear and present. The voices of the special interests are persistent and pervasive. The national interest is less clearly heard.

H.R. 4800, the House trade bill which pased overwhelmingly on May 22, is a blueprint for closing markets. Frankly, it is a bill based on election-year politics. It would halt and reverse the progress in international trade built up over the past 40 years. It is sure to increase political and economic tensions around the world. H.R. 4800 offers trade restriction as the solution without understanding the true nature of the trade problem.

What Is the Trade Problem?

I won't stand here and tell you that there is no trade problem. There *is* a problem. We are experiencing the largest trade deficits in our history. During the past 2 years, the deficit set a record virtually every month. That pattern may not yet be broken. These massive trade deficits, and the even larger Federal budget deficits, are serious and must not be ignored. Among other factors, these deficits have eroded the important coalition we have had in this country for freer, more open trade. Deficits of this magnitude are almost certainly not sustainable.

We must take action to deal with our deficits and the concerns they generate. We must rebuild that coalition of farmers, consumers, businessmen, politicians, academics, and—yes—even Washington bureaucrats that has shaped our open trading policies. And, at the same time, we must guard against false solutions that will make matters worse.

The American economy has performed well over the last 4 years. Certain industries and certain areas of the country are in difficulty, but their problems are set in a powerful pattern of progress. Overall, we are better off than we were 6 years ago. Prospects are that we will be still better off this year and the next. Deregulation, market freedom, private sector incentives, and less intrusive government have produced this progress. We have rising incomes, new jobs, low inflation, productive investment, affordable housing, lower taxes, dynamic capital markets, and an efficient farm sector.

Why, I wonder, are some now tempted to take trade policy in the opposite direction? Why intervene in international markets when our domestic successes spring from less intervention? Why close markets when our postwar heritage of opening them has stimulated the greatest expansion of economic well-being in the history of the

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world? Why add friction and increase the risk of conflict between nations?

Is market closing the best way to deal with our trade imbalance? Are the proponents of H.R. 4800 correct? More to the point, would it even work?

Let's look at the five issues most often raised in today's trade debate.

- Why do we have a trade deficit?
- How can trade policy reduce the deficit?
- Do imports cost jobs?
- What is fair trade?
- Do we have a trade policy?

Cause of the Trade Deficit

First, why do we have a trade deficit?

The fundamental cause is that during the last 3 years domestic investment has substantially exceeded domestic saving. The difference—that portion of our total investment financed by foreign savings—is equal to the deficit in our trade in goods and services. Only when we bring domestic investment and domestic saving back into balance will we bring our trade account back into balance.

To understand how the present situation arose, we have to look again at our record of economic performance. The U.S. economy has created 10 million new jobs since 1981; investment was necessary to create those jobs. In the recovery of the 1980s, investment contributed more to growth than in any previous postwar recovery. Real business investment as a share of real GNP [gross national product] reached a postwar high. The American people, collectively, with renewed confidence in the economic future, invested their savings at home rather than lending abroad. American consumers also fueled economic growth through their spending.

For its part, the Federal Government embarked on a monumental effort to rebuild our nation's defenses—a public investment in our future security. However, while private savings have exceeded total private investment, the Federal Government has been spending much more than its income. This draws off savings from the private sector.

How is it possible for the economy as a whole to spend more than it earns? It's simple: others somewhere in the world spend less than they earn and invest the difference the America. We are able to support our ambitious investment program, public and private, with an inflow of savings from abroad. That inflow of savings must be accompanied by a parallel influx of goods.

To reduce the trade deficit, we must restore a better balance between the demand for capital—our public and private investment—and the domestic supply of capital—the savings generated by households, businesses, and government. We can invest less or save more. The choice is ours.

A Trade Policy Remedy?

What role can trade policy play in all of this?

Trade policy does not significantly affect the trade balance. Let me repeat that: trade policy does not significantly affect the trade balance.

To be sure, some trade policy actions may cause minor shifts in previous saving and investment patterns. But trade restrictions do not affect the fundamental cause of the trade deficit: the inability of domestic savings to finance domestic investment. Trade restrictions can only divert resources to protected sectors of the economy and away from dynamic sectors that are typically left unprotected. When we restrict imports, we act not so much against foreign producers as against our own domestic consumers, our industries that rely on imported materials, and our farmers and industries who need foreign markets.

Trade and Jobs

Well, what about jobs? Don't imports cost Americans their jobs? Don't exports create jobs? These are tough questions, not because the answers are complex or remote but because wrong answers are so prevalent, appealing, and convenient.

There is no doubt that fewer Americans are engaged in producing VCRs, or color televisions, or cameras, or even automobiles and steel because we import these items. There is also no doubt that more Americans are engaged in producing aircraft, computers, advanced electronics, and agricultural products because we export them. But it is a fundamental truth that trade policy affects only the composition of employment, not its total level. You can safely dismiss any analysis that states that a particular trade restriction will "save" a certain number of American jobs. Such restrictions do not save jobs in the overall but shift employment from our most dynamic industries to less productive sectors.

Fairness and Market Access

But what about fairness? What about the "level playing field" our exporters have a right to expect? Americans value fairness—it is one of our finest national attributes. If we are not being treated fairly, we will react, whether our trade is in surplus or in deficit.

Without doubt, there are unfair trade practices in the world. Although we do not necessarily agree, even some of our own practices are perceived as unfair by others. Developing countries complain that we have cut our sugar import quotas from 2.2 million tons in 1985 to 1.7 million tons this year; our textile imports are subject to tight controls; the new farm bill expands subsidies for agricultural exports; we recently restricted imports of certain wood products; and we restrict steel imports from 17 countries and Europe. The list goes on. As someone said, purity and virtue are hard to find in the world of trade.

There is another aspect of fairness that deserves attention. Too often, the unspoken definition of fairness is "our industry always wins." Loss of market share abroad translates into an unfair practice by a competitor. The trade deficit is seen as proof that American business is facing unfair competition. Fairness does not mean that every U.S. industry always prospers. Fairness means we all play by the same rules. Americans don't want guaranteed success; but they do insist on the opportunity to succeed.

But where unfairness exists, how should we deal with it? Retaliation—restricting access to the U.S. market—comes quickly to mind. There are two problems with retaliation.

First, it hurts our own economy.

Second, it invites an escalating and dangerous spiral of counterrestrictions.

Nevertheless, despite the risks, retaliation may be necessary in some cases. When it is, we will act and have done so.

What we shouldn't do, though, is base our policy on the concept of retaliation. The most effective approach to foreign unfair trade practices is to confront them directly: to demonstrate the unfairness and secure change through negotiation. This course serves our broader economic interests and those of the world trading community by creating new possibilities for growth and enhanced competition. Unlike retaliation, it is true to the principles of economic freedom that have served us so well in the past. Success has not

been and will not be instantaneous, since the political forces of protectionism are at least as strong abroad as they are in this country. But we have made progress, real progress.

American exporters deserve the full effort of their government to assure them of as open and efficient a market as possible when they set out to compete. The President has pledged that effort. But we must not bind ourselves with a web of trade restrictions. As in the domestic economy, our efforts must be devoted to greater freedom, not greater government.

The Administration's Trade Policy: Aims and Actions

What is our trade policy? In the tradition of every American President since F.D.R., President Reagan stands for free trade and open markets. That is our policy framework. Our objectives are clear: to pry open foreign markets, to tear down trade barriers, and to eliminate unfair trade practices.

- The United States has taken the lead in pushing for a new round of international negotiations that will be launched this fall. Our objective is to strengthen existing trade rules and extend them to areas such as agriculture, services, intellectual property, and investment which have, until now, escaped meaningful—or any—international discipline. Multilateral negotiations in the GATT [General Agreement on Tariffs and Trade] are our best hope for establishing a broader, level playing field free of the holes we have all dug for ourselves in the past.
- Responding to a Canadian initiative, we have just embarked on an important and historic initiative with Canada, our largest trading partner. We are engaging in comprehensive talks to establish free trade between our two countries. The objective of these talks is to reduce or eliminate barriers in a broad array of trade and investment areas. An agreement of this type will be an engine of growth for the economies of both countries.
- In a series of talks with the Japanese Government, we have agreed on the removal of barriers to sales in Japan of telecommunications gear, wood and paper products, pharmaceuticals and medical equipment, and electronic components. In the near future, we will discuss ways to enhance market access in a new sector which includes automobile parts.
- We are pressing the European Community to offer us adequate and fair compensation for damage to our agricultural exports caused by the recent expansion of the Community to include Spain and Portugal.
- We are negotiating with Korea to improve opportunities for our insurance companies to sell in Korea and to obtain better patent and copyright protection there. Similarly, we are pressing Brazil to administer its laws regarding computers and related equipment so as not to disadvantage unfairly U.S. investors and exporters.

This is only a partial list, but it illustrates that positive, market-opening actions have been taken and are underway to eliminate unfair trade practices and expand market access for competitive U.S. exports of both goods and services. The record shows that negotiation can open markets.

We have also made important strides on domestic and multilateral measures that will help attack the fundamental cause of the trade deficit.

- On the domestic front, Congress has tackled its responsibility to discipline spending by the Federal Government by passing the Gramm-Rudman-Hollings amendment. By 1990, the Federal Government's voracious appetite for American savings will be curbed.
- Also, the Senate has passed a tax reform bill that will enhance the incentives to work, to save, and to invest in productive activities.

These two measures alone will significantly enhance the competitive position of the United States and release resources to the private sector. They will also contribute to a better balance in our external accounts—a lower trade deficit—by reducing the internal imbalance between saving and investment. They represent major achievements in the making.

Abroad, we are working with our trading partners on monetary matters. Exchange rates have shifted to reflect better fundamental economic conditions. The dollar has moved to a level that reflects our commitment to put our economic house in order and restores the competitiveness of American industry and agriculture. Agreements reached last September at the Plaza Hotel and in May at the Tokyo summit promote greater stability in exchange rates.

American Leadership

The trade policy debate in Washington is serious and disturbing. The trend in the Congress—at least in the House of Representatives—runs counter to the policy direction that has revived the American economy in the 1980s and to the course of American trade policy over nine administrations, Democratic and Republican. It contradicts the principles of economic and political freedom that have been the basis of the strength and prosperity of this country.

The United States has been in the forefront of the battle for economic freedom, just as we have been at the front lines in the struggle for political freedom. Will the United States maintain its leadership role in the global economy and continue to lead in the pursuit of freer trade and more open markets?

The importance of American leadership to the progress of freedom was emphasized by the Prime Minister of Singapore, Mr. Lee Kuan Yew, before a joint session of our Congress last fall. Let me conclude by quoting from his speech:

> If, because of domestic problems, the United States loses the will to maintain open and fair trade, protectionism and retaliation will shrink trade and so reduce jobs. Is America willing to write off the peaceful and constructive developments of the last 40 years that she has made possible? A replay of the depression of the 1930s, which led to World War II, would be ruinous for all. All major powers in the West share the responsibility for not repeating this mistake. But America has the primary responsibility, for she is the anchor economy of the free market economies of the world. In your hands, therefore, lies the future of the world.

Our friends are calling on us to lead—to remain true to the economic and political values that form the bedrock of our way of life. We need the vision, statesmanship, and—yes—courage that inspired the Founding Fathers 210 years ago. If we are true to our principles, we can lead the world to a future of progress and prosperity. ■

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